Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

Author:	Aanestad	Analyst:	Roger Lackey	Bill Number:	AB 2720
Related Bills:	None	Telephone:	845-3627	Introduced Date:	02-22-2002
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Medical & Health Service Costs Credit For Senior Citizens Whose HMO Benefits Were Terminated

SUMMARY

This bill would allow a senior citizen whose HMO benefits were terminated a credit equal to the amount paid for health and medical services.

PURPOSE OF THE BILL

It appears the intent of this bill is to assist senior citizens who lose their HMO medical coverage.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately and operative for taxable years beginning on or after January 1, 2002.

POSITION

Pending.

Summary of Suggested Amendments

Department staff is available to assist the author's office in resolving the concerns addressed below.

ANALYSIS

FEDERAL/STATE LAW

Existing federal and state law allows individuals to deduct certain expenses, such as medical expenses (which must exceed 7.5% of AGI), charitable contributions, interest, and taxes, as itemized deductions. Expenses for the production of income and certain employee business expenses are considered miscellaneous itemized deductions and must exceed 2% of adjusted gross income (AGI) to be deducted.

There is no federal or state credit comparable to the credit proposed by this bill.

Board Position:			Department Director	Date
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THIS BILL

This bill would allow a credit equal to the costs paid or incurred by a qualified senior citizen for medical and health services.

A "qualified senior citizen" would mean any person that before the close of the taxable year was at least 60 years of age and had his or her HMO medical coverage terminated. The termination would be as a result of the HMO's cancellation of services in a specified area or to a specified class of beneficiaries.

"HMO" would mean a public or private organization organized under the laws of this state that:

- Provides or makes available health services to its enrolled participants, including at least certain basic health services, to wit: usual physician services, hospitalization, laboratory, X-ray, emergency, and preventative services, and out-of-area coverage.

- Is compensated on a predetermined periodic rate basis, except for co-payments, for providing the basic health care services listed above.

- Provides physician services primarily thru physicians who are employees or partners of the organization, or thru arrangements with individual physicians, or a group of physicians organized on group practice or individual practice basis.

Any excess credit could be carried forward to subsequent taxable years until exhausted.

IMPLEMENTATION CONSIDERATIONS

It is not clear what "medical and health services" would include. It would be difficult for both the taxpayer and the department to determine the appropriate credit if "medical and health services" is not clarified.

This credit would apply to any "qualified senior citizen" regardless of whether they received treatment in this state or whether the HMO is located in this state. Clarification on these issues is necessary to properly implement and verify the credit.

TECHNICAL CONSIDERATIONS

Although "HMO" is defined in the bill, the term Health Management Organization is never used. Generally, the term or phrase that makes up the acronym is stated prior to using the acronym.

This bill would define a qualified senior citizen as a "person" that meets certain criteria. For purposes of this bill, it may be more appropriate to refer to the qualified senior citizen as an "individual" rather than a person. As used in the Revenue and Taxation Code "person" could include a partnership or an entity other than an individual taxpayer.

OTHER STATES' INFORMATION

The income tax laws of *Illinois*, *Massachusetts*, *Michigan* and *New York* were reviewed because their laws are similar to California. *Illinois, Massachusetts, and New York* had no credits similar to the one proposed by this bill. *Michigan* had a senior related credit as described below.

Michigan allows a credit for the unreimbursed cost for prescription drugs. The credit is available to individuals 65 or older who meet prescribed income limitations. The credit is not claimed against income tax liability, but rather is claimed on another form and refunded to the individual.

New York allows a long-term care insurance credit. The credit is equal to 10% of the premiums paid for long-term care insurance.

FISCAL IMPACT

Once the implementation considerations are resolved, this bill would not significantly impact the department's costs.

ECONOMIC IMPACT

<u>Revenue Estimate</u>

This bill is estimated to impact revenue as shown in the following table.

Revenue Losses Tax Years Beginning After December 31, 2001 Enactment Assumed After June 30, 2002 ($ Millions)			
Fiscal Year	2002-03	2003-04	2004-05
	(Minor)	(Minor)	(Minor)

Minor = <$1 million.

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this measure.

<u>Revenue Discussion</u>

For this analysis, it is assumed that an HMO cancellation of services to specified class beneficiaries refers to Medicare Managed Care enrollees. Since an HMO Medicare qualified enrollee can still receive medical and health services directly through Medicare, there would be minimal out-of-pocket expenses incurred for services received by individuals. Therefore, this bill as introduced would have a minor revenue impact.

In addition, many seniors would have the option to join other HMOs, or some other insurance provider, or to buy supplemental insurance, in order to continue health coverage.

ARGUMENTS/POLICY CONCERNS

Current law allows a taxpayer to deduct medical expenses as an itemized deduction. Conflicting tax policies come into play whenever a credit is provided for an item that is already deductible as an expense item. Providing both a credit and allowing a deduction would have the effect of providing a double benefit for that item.

Credits generally are provided as a percentage of amounts paid or incurred. This bill would allow a 100% credit, which is unprecedented.

This bill does not specify a repeal date or limit the number of years for the carryover period. Credits typically are enacted with a repeal date to allow the Legislature to review their effectiveness. However, even if a repeal date were added, the department would be required to retain the carryover on the tax forms indefinitely because an unlimited credit carryover period is allowed. Recent credits have been enacted with a carryover limitation since experience shows credits are typically used within eight years of being earned.

This credit is limited to taxpayers that are 60 years of age or more. As a result, this credit would provide inequitable treatment to taxpayers younger than 60 who have lost HMO coverage.

The credit would be allowed for medical expenses paid or incurred either inside or outside California.

LEGISLATIVE STAFF CONTACT

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